



CITY COUNCIL STUDY SESSION REPORT

MEETING DATE: February 9, 2010

ITEM NUMBER:

SUBJECT: FISCAL YEAR 2009-2010 MID-YEAR BUDGET REPORT

DATE: FEBRUARY 4, 2010

FROM: FINANCE DEPARTMENT/FINANCIAL PLANNING

PRESENTATION BY: BOBBY YOUNG, BUDGET & RESEARCH OFFICER

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RECOMMENDED ACTION:

1. Receive and file the Fiscal Year 2009-2010 (FY 09-10) Mid-Year Budget Report.
2. Provide information to staff regarding Council's expectations for next year's budget.

BACKGROUND:

The focus of the mid-year budget review presentation is primarily the City's General Operating Fund revenues and expenditures. The vast majority (over 81%) of the City's activities are accounted for within this fund. Other special revenue fund budgets, such as the Gas Tax, Community Development Block Grant (CDBG) or HOME Funds, do not usually require adjustments at mid-year due to the specific nature of the resource allocations and program requirements. When revenues for these special revenue funds are not fully expended during the year, balances are carried forward for re-appropriation in the subsequent years' budget process. Adjustments to other funds are submitted to Council on as needed basis periodically throughout the year.

The budget is the City's spending plan. The City Council adopted the FY 09-10 budget on June 16, 2009. At that time, the world's economy was contracting and the City's revenues were decreasing. Therefore, included in the adoption of the FY 09-10 budget was a 10 Point Budget Management Plan to help reduce expenditures in light of the worsening economy and declining revenues. If all aspects of the 10 point plan were realized, the estimated impact was \$20.1 million. To varying degrees, the City has taken action on all 10 points of the plan. A summary of each is detailed below.

Unfortunately, since adoption of the budget (June 2009), the economy has continued to decline. This is marking the second full year the economy has been in a recession period and the City having to address financial concerns. Staff is continuing to analyze the impacts to the City and has made recommendations below. Also, as of now, the Governor's proposal for the State's Budget does not appear to have any short term General Fund impacts. However, it will continue to be an area of concern until a formal budget is adopted.

ANALYSIS:

The following is an update on the implementation of the 10 point Budget Management Strategies.

- 1. Reduce department operating budgets by an additional 5% for an average reduction of 10% by departments from the prior fiscal year. Original estimate - \$6,318,134.**
 - From an amended budget in FY 08-09 of \$120.9 million to an adopted budget in FY 09-10 of \$102.4, the City reduced the General Fund budget by \$18.5 million or 15.30%. Since items #2, #3 and #7 were all assumed at the time of adoption, with the removal of those items the final adopted amount would have been \$107.5 million and the reduction would be approximately \$13.4 million or 11.08%
- 2. Negotiate reduction in employee compensation equating to approximately 5% of salary. Original estimate - \$3,623,663.**
 - The City successfully negotiated a reduction in employee compensation equal to 5% by way of furloughs for all employees except Costa Mesa Firefighters Association (CMFA) employees. Although the furloughs did not start simultaneously with the fiscal year, the furloughs will continue for 26 pay periods (the equivalent of one fiscal year) for a total savings of \$3.0 million. It is anticipated savings of approximately \$2.5 million will be recognized in FY 09-10, therefore the remaining \$500,000 of savings will be recognized in FY 10-11.
 - Since the City negotiated a new contract with CMFA, the savings from that plan will happen as soon as retirements take place and positions are left vacant. With 12 positions held vacant at an approximate budget amount of \$150,000 each for an annual savings of \$1.8 million, the savings will offset the cost of the retirement plan change from 3@55 to 3@50 (approximately \$700,000 per year) for a net savings of approximately \$1.1 million a year.
- 3. Reduction of \$1 million in non-reimbursable overtime for Police and Fire departments. Original estimate - \$1,000,000.**
 - The Police Department is taking a strategic approach to reduce non-reimbursed overtime. Because the department is also having to schedule furloughs, management - while ensuring all basic services are still provided - is allowing overtime only when absolutely necessary.
 - The Fire Department has shifted to a variable staffing model as per the new contract because of the current reduction of staff (as discussed in #4 below), which should produce a reduction in overtime.
- 4. Negotiate suspension of minimum manning requirements in the Fire Department in order to accomplish the aforementioned reduction in overtime. Original estimate - \$0.**
 - The City successfully negotiated a reduction in minimum manning requirements in the Fire Department from the previous level of 32 personnel per shift. As per the new contract with CMFA, current variable staffing levels are at 30 per shift and upon the implementation of 3@50 and the close of a Retirement Incentive window, staffing will then be at a minimum 28 per shift. The current change to variable staffing is producing a savings in overtime by giving the shift command the ability to not immediately backfill for vacant positions because of retirements

or vacation/sick leave. The reduction comes from having a staff of 3 (instead of 4) fire personnel on 2 of the 8 apparatus.

5. Seek Federal Stimulus funding for ten police officer positions to be eliminated due to Police Department budget reductions. Original estimate - \$1,052,010.

- Unfortunately the City of Costa Mesa was not selected for Federal Stimulus funding for Police Officers in the COPS Hiring Recovery Program (CHRP) by the Department of Justice (DOJ) thereby reducing estimated revenues by \$1.05 million (see below). This federal program had funding of \$1 billion and was reported to have received applications in excess of \$7 billion. Although the City was not initially selected, staff is continuing to track this grant in case more funding becomes available.

6. Offer PERS Retirement Incentive to create vacancies to (1) reduce the number of personnel that may be laid off as a result of reductions in departmental operating budgets and (2) create additional vacancies needed for budgetary purposes (assumes total of 50 employees opting to retire of which 25 positions would be eliminated). Original estimate - \$3,485,000.

- The City began offering the Retirement Incentive of 2 years additional service credit on August 18, 2009. The window to take advantage of the incentive closed December 31, 2009. A total of 54 employees took advantage of the incentive. Preliminarily, management staff has determined 40 positions can remain vacant. The attrition savings (budgetary impact) from these 40 positions is estimated to be \$3.6 million.

7. Suspension of the Retiree Health Savings (RHS) Plan (contributions are comprised of 1% by employer and 1% by employee). Original estimate - \$508,764.

- The City successfully negotiated the suspension of the RHS plan with all represented and non-represented employees for a period of 26 pay periods. The suspension began with the pay period of August 29. Since the suspension did not start at the beginning of the fiscal year, it is estimated the City will recognize a savings of about \$420,000 in FY 09-10 and the remaining \$80,000 in FY 10-11.

8. Implement various cost recovery programs including resident EMS fees, inspection fees, and Police and Fire Cost Reimbursement Fees. Original estimate - \$959,700.

- On May 5, 2009, City Council authorized staff to implement a Motor Vehicle Accident Cost Recovery Program, which seeks reimbursement of staff time and materials, mostly by the Fire Department, when responding to an auto accident. It is estimated this new program will generate approximately \$180,000 in new revenue for the City's General Fund.
- On June 2, 2009, City Council authorized staff to implement a Hazardous Materials Disclosure Late Fee, which is estimated to generate approximately \$4,000 in new revenue for the City's General Fund.
- Also on June 2, 2009, City Council adopted a resolution for Fire Prevention User Fees and Charges which established a flat rate for those fees rather than the 1997 Uniform Administrative Code tables. Because of this change in calculation, an estimate of the increase in revenue could not be completed.

- Other programs proposed but not adopted: Apartment Inspection Fees, Business Inspection Fee, and modification of Emergency Medical Services (EMS) billing without regard to residency.
 - The total estimated increase in revenue due the change of fees is approximately \$180,000. Analysis of the Fire Prevention User Fees will be completed when more data is available.
- 9. Renegotiate/extend the Golf Course Operator's agreement for a greater share of the revenues and institute formula adjustments to the greens fees. Original estimate - \$244,850.**
- The City successfully renegotiated the Golf Course Operator's agreement with Mesa Verde Partners with the approval of City Council on June 16, 2009. The new agreement provides that 2.5% of greens fees be directed to the City's General Fund – approximately \$122,500, and that the City receive one half of the existing balance available for golf course capital improvements – approximately \$175,000, for a total increase of revenues in FY 09-10 of \$297,500.
- 10. Utilization of undesignated unreserved General Fund Balance. Original estimate - \$2,900,000.**
- As adopted, the projected use of fund balance was \$4.65 million. Some of the items produced a savings (items #1, #2, #3, #4, #6, #7, parts of #8, #9) while others did not (items #5 and parts of #8), the resulting projected use of fund balance would have been \$3.0 million (see below).

As mentioned the original estimated impact of the 10 Point Plan was \$20.1 million. Now that action has been taken on all points, staff estimates the budgetary impact to be \$22.0 million.

Based on staff's analysis of the current year's operating revenues and expenditures and, based on information and input provided by all departments, staff recommends the following adjustments to the FY 09-10 budget:

Revenues

Sales Tax: Analysis of the first six months of sales tax receipts shows a continued decline of 7.1% compared to first six months of the prior fiscal year (08-09). At this time last year, the 08-09 fiscal year was down 14.0% compared to the first six months of 07-08. The total reduction in sales tax revenue for the first six months compare to 07-08 is a decline of 21.1%. Sales tax data for the past holiday season will not be available until the first week of March, 2010. However, based on national economic data, it is estimated retail sales only increased by about 1% during the fourth quarter of 2009. Unfortunately, this is not enough to offset the continued decline in auto sales which is about 17% of overall sales tax collections. The State Department of Finance has estimated the statewide decline for FY 09-10 to be 7% compared to FY 08-09.

Another aspect of the City's Sales Tax revenue is the Triple Flip Backfill payment. These payments are estimated by the State on an annual basis, and adjusted the following year for any over or under payments based on actual sales activity. The State Department of Finance has estimated this decline for FY 09-10 to be 27.6% compared to FY 08-09.

Based on analysis of the first six months and the fact the City is continuing to experience a decline, it is recommended to reduce the Sales Tax Revenue projection by \$3.81 million and Sales Tax Backfill projection by \$2.25 million for a total reduction of \$6.06 million.

Transient Occupancy Tax (TOT): Analysis of the first six months of transient occupancy tax collections shows a continued decline of 15.9% compared to first six months of the prior fiscal year (08-09). At this time last year, the 08-09 fiscal year was down 12.5% compared to the first six months of 07-08. The total reduction in sales tax revenue for the first six months compare to 07-08 is a decline of 28.4%. This decrease is reflective of the continued decline in discretionary income generally used for leisure travel due to the recession.

Based on the analysis of the first six months and the fact the City is continuing to experience a decline in TOT collections, it is recommended to reduce the Transient Occupancy Tax revenue projection by \$1.14 million.

Further reductions in revenue estimates include \$598,000 for Red Light Camera, \$500,000 for Investment Earnings, \$1.05 million in Other Reimbursements due to the lack of Federal Stimulus funding for Police Officers (item #5 of the 10 Point Plan). Total reductions to all revenue accounts is \$7.1 million.

Expenditures

Each department has provided feedback on its year-to-date budget performance as projected through the fiscal year-end. In total, expenditures across all departments are projected to stay within the current amended appropriations for this fiscal year, except as noted below.

As it relates to the implemented furlough program and suspension of the RHS program, as previously discussed, because both did not start until about September 1, 2009, the City will only realize 10 months of savings and the remaining 2 months would be recognized in FY 10-11. The budgetary impact of the delay in savings is the inclusion of \$589,800 in appropriations to the 09-10 budget.

Included in the FY 09-10 adopted budget was an amount to begin funding the City's retiree medical obligation. However, given the City's financial constraints, the decision was made to continue funding these obligations on a pay-as-you-go basis rather than prefunding. Based on this decision, appropriations for the Retiree Medical account can be reduced by \$650,000.

Also, since the City's Red Light Camera system has only been operating at two intersections, total payments to the vendor are expected to be less. It is recommended the appropriation for these services be reduced by \$800,000.

The estimated reduction in FY 09-10 appropriations as a result of the PERS 2 year Retirement Incentive is approximately \$3.6 million. This is based on the fact that a total of 53 employees took advantage of the program and it is currently estimated a total of 40 positions will be left vacant for the remainder of the year.

It is also recommended to increase both revenue and principal and interest appropriations for the Police Facility Expansion debt service payment that was not included in the budget. Since the project was completed under budget, it was anticipated the remaining funds from the project would be used to make the debt service payments. The City will be using the extra funds to make the payment, however must record both the expenditure and offsetting revenue in the amount of \$2,086,004 in the General Fund.

Summary

The FY 09-10 budget was adopted with a planned appropriation from General Fund available fund balance of approximately \$4.6 million. However, this amount did not include any savings from the PERS 2 Year Retirement Incentive. Following adoption of the budget and during the first six months of the fiscal year, the economy appears to still be in a recessionary period. This recession continues to impact two the City's largest revenue sources, Sales Tax and Transient Occupancy Tax.

Exhibit A summarizes revenues and appropriations both as adopted and as revised. The net result of these reductions in revenue estimates and appropriations will increase the amount of the planned appropriation from General Fund available fund balance from \$4.6 million to \$9.3 million.

ALTERNATIVES CONSIDERED:

No alternatives were considered.

FISCAL REVIEW:

The attached Exhibit A summarizes the proposed adjustments in revenues and expenditures to the current year's adopted operating and capital improvement budget reviewed herein. Including the recommended adjustments, the estimated use of General Fund fund balance has increased from \$4.6 million to \$9.3 million.

LEGAL REVIEW:

No legal review is required for this item.

CONCLUSION:

In June 2009, Management proposed and the City Council adopted a budget for FY 09-10 that included a 10 Point Budget Management Plan. To varying degrees, the City has taken action on all 10 points. While only a couple did not produce a savings, many of them have been successful. Even though the City has worked diligently to reduce expenditures, the continuing recession has further eroded to City's revenues. Over the first six months of the fiscal year, Sales Tax has further decreased by 7.1% and Transient Occupancy Tax has decreased by 15.9%. It is projected that decreases in these two revenue sources will continue, leading staff to recommend reducing the projected estimates for all revenue sources by \$7.1 million.

Staff is also recommending a decrease of budgeted appropriations in the amount of \$2.4 million. This decrease is mostly related to the expected attrition savings from the PERS 2 Year Retirement Incentive. It also includes a reduction for Red Light Camera expenditures and prefunding of the City's Retiree Medical Program.

Staff is committed to ensuring the City continues its conservative fiscal practices; adopts sound, responsible, financial plans; and maintains its high-level of service delivery to the community in the most cost-effective and efficient manner possible. In addition, staff is now compiling departmental budget requests for the next fiscal year. As such, staff requests that Council provide feedback regarding its priorities and expectations for FY 10-11 to help guide the development of the proposed budget.

BOBBY YOUNG
Budget & Research Officer

ATTACHMENTS: Exhibit A – Mid-Year Budget Report Summary

Copy to: City Manager
All Department Directors